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SUBJECT: EUROPE FINANCIAL AND ECONOMIC REPORT:
6th, 2009

March

FINANCIAL SERVICES: UPCOMING ISSUES /EVENTS

Capital Requirement Directives (CRD):

[11](#). (SBU) On March 9, the ECON Committee of the European Parliament (EP) will vote on amendments to the CRD report. It is likely that there will be amendments passed asking the Commission to submit proposals to enhance transparency of the OTC derivatives market, including mandatory central counterparty clearing, by December 2009, though possibly not to raise capital requirements for non EU-cleared CDSs at this time.

Credit Rating Agencies (CRAs):

[12](#). (SBU) On March 9, the ECON Committee of the European On March 9, the EP ECON Committee is set to discuss amendments to the report on Credit Rating Agencies. MEP Gauzes (French, Conservative) will also start negotiations with the Council and the Commission to reconcile different approaches by the three institutions on the issue.

EUROGROUP / ECOFIN:

[13](#). (SBU) On March 9, the ECON Committee of the European Eurogroup Finance Ministers will meet on March 9 and the ECOFIN will meet on March 10. This week's ECOFIN will be almost entirely devoted to preparing key policy documents for the spring European Council of March 19 and 20. The Council is expected to endorse the main lines of the EU's position for April's G-20, as well as the Commission's assessment on the 2009 Stability and Convergence Programs.

European Council:

[14](#). (SBU) On March 9, the ECON Committee of the European Leaders will meet for the Spring European Council on March 19 and 20. They will work on a common EU position for the upcoming G-20 meeting. Leaders are also expected to endorse the country-specific recommendations for member States on economic and employment policy.

FINANCIAL SERVICES: RECENT EVENTS:

Berlin mini-G-20 sees EU leaders move towards increased financial regulation and oversight:

[15](#). (SBU) On March 9, the ECON Committee of the European On February 22, leaders from Britain, France, Germany, Italy, Spain, the Netherlands, Luxembourg (representing Euro area nations), and the Czech Republic (current EU Presidency) met in Berlin with

representatives of the European Commission (EC) and of the European Central Bank to lay the groundwork for Europe's position for April's G-20 meeting, and agreed on the following principles:

- * Strengthen supervision and regulation for financial markets, hedge funds, rating agencies;
- * Clamp down on tax havens with increased capital requirements for off shore centers;
- * Implement counter-cyclical measures for banks, and limit bonus payments;
- * A sustainability charter, reducing economic imbalances and stabilizing financial markets;
- * Empower the IMF and the FSF to implement the financial action plan; and
- * Doubling the financial resources for the IMF.

COREPER agrees to a "general approach" on the Draft CRA Regulation:

16. (SBU) The Permanent Representatives of the EU Member States (COREPER) agreed to a "general approach" that confirms the Commission's intention to assign CRAs supervisory authority to the Member States. The Council proposal would allow EU-registered CRAs to endorse ratings prepared by non-EU-registered CRAs, an approach already envisaged by the EP's report. The latest Council document does not introduce a requirement for determining regulatory equivalence between jurisdictions. The EP is likely to disagree with the Council document on a number of issues, including the registration and supervisory arrangements and the lack of a regulatory equivalence.

De Larosiere proposes changes to EU supervision; the Commission pledges to implement by 2010

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Capital Requirement Directives (CRD):

17. (SBU) On February 25, Jacques de Larosiere released his report on the future of EU financial supervision. The key recommendations include a revision of Basel II to reduce pro-cyclicality, a reform of mark-to-market and of IASB governance, and an overhaul of the European macro and micro financial supervision through the creation of a European Systemic Risk Council (ESRC) to improve macro-prudential supervision, and a European System of Financial Supervision (ESFS), to improve micro-prudential supervision. On the basis of the report, the Commission unveiled on March 4 the Communication "Driving the European recovery", broadly endorsing de Larosiere's recommendations, and announced proposals on liquidity risk and excessive leverage, and executive pay. A roadmap will be presented by the end of May for discussion at the June European Council, and formal legislation will be sent to Parliament in the fall for an adoption target of 2010.

Conference on hedge funds confirms EU's intention to legislate

18. (SBU) On February 27-28, the Commission organized a two-day conference as part of the Commission's consultation on the hedge fund and private equity industries. MEPs from across the political spectrum noted that regulation is coming, though Commissioner McCreevy offered little specific policy indication, except to note his awareness of the highly transnational character of both hedge and private equity funds, and of the need for regulation not to stifle innovation. He noted that such regulation would therefore be targeted at market failures, with investor protection provisions taking into account the professional quality of both industries' investor base.

EC guidance on impaired assets

19. (SBU) On February 25, the European Commission published a Communication providing guidance to Member States in dealing with impaired assets. The guidance outlines various possible methods (asset purchase, "bad bank" scenarios, asset insurance schemes,

swaps guarantees, or hybrid models), and explains the budgetary and regulatory implications of asset relief measures. The design of the asset relief scheme remains the responsibility of Member States. The Communication details how State aid rules on such measures would be applied. Guidelines on the treatment of impaired assets

ECONOMICS / FINANCE: UPCOMING ISSUES / EVENTS

G-20 Finance ministerial:

¶10. (SBU) On March 14 and 15, the G-20 Finance Ministers will meet in London to set the stage for the April 2 G-20 meeting.

ECONOMICS / FINANCE: RECENT EVENTS:

ECB cuts interests rates by 50 basis points, BoE gets authority to print GBP150bn

¶11. (SBU) On March 5, the ECB cut its main refinancing rate by 50 basis points to 1.5% and revised down its economic growth forecasts for this year and 2010. ECB President Trichet signaled that 1.5% is not necessarily the lowest level to which the ECB can cut its key rate, fuelling speculations that the ECB could cut interest rates again next month. Meanwhile, Bank of England Governor Mervyn King received authority to print as much as GBP 150bn (\$212 billion), to execute his strategy of quantitative easing. .

Commission assesses a second tranche of convergence programs (Italy, Luxembourg, Portugal and Lithuania)

¶12. (SBU) On March 9, the ECON Committee of the European Commission assesses a second tranche of convergence programs (Italy, Luxembourg, Portugal and Lithuania) The assessment by the Commission of a second tranche of Stability and Convergence Programs (SCPs) last week yielded no new recommendations for Excessive Deficit Procedures (EDP), but the analysis found that budgetary positions are projected to deteriorate markedly in 2009 in Italy, Luxembourg and Portugal reflecting, in

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Capital Requirement Directives (CRD):

the latter two countries, the significant economic stimulus packages adopted. The Commission noted that Italy's recovery measures are budgetary neutral, in line with the country's very high debt ratio. For Lithuania, the Commission considers that the restrictive fiscal stance planned for the whole program period is an appropriate response to the existing economic imbalances, but still sees significant downside risks to achieving these objectives.

Commission authorizes controversial French proposal to aid carmakers.

¶13. (SBU) On February 28, the EU competition authorities authorized the French plan to support the French automotive industry that caused tension between France and the Czech Republic. The Commission's authorization came in the wake of the March 1 extraordinary European summit and after having received written assurances from the French government that it will not make aid to car manufactures conditional to a repatriation of manufacturing activities or to a commitment to use national vendors.

Extraordinary meeting of EU Leaders:

¶14. (SBU) EU leaders met in Brussels on March 1 to address growing concerns on the financial stability of the Central and Eastern European (CEE) Member States, and to discuss the possibility of a pan-European rescue plan for the auto industry. EU leaders rejected requests for assistance for CEE to be given on a regional basis,

opting for a country by country approach, and passing over a proposal by Hungary assistance of 180bn (\$228 billion) for the newer Member States.

Almunia sees European economic outlook worsening

¶15. (SBU) Speaking in front of a leading Brussels think-tank on March 3, Commissioner Almunia said that the economic outlook for Europe has worsened compared to the January interim forecasts, and warned of their possible downward revision. Commissioner Almunia also indicated that the impact of European Economic Recovery Plan measures should begin to be felt in the second half of 2009, with recovery beginning in 2010.

MURRAY